REPORT OF EXAMINATION
OF THE

BUSINESS ALLIANCE INSURANCE COMPANY

AS OF
DECEMBER 31, 2009

Filed June 24, 2011

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San Francisco, California
March 9, 2011

Honorable Dave Jones
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

BUSINESS ALLIANCE INSURANCE COMPANY

(hereinafter also referred to as the Company) at the primary location of its books and records, One Park Avenue, New York, New York 10016. The Company's statutory home office is located at 900 Cherry Avenue, San Bruno, California 94066.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2005. This examination covers the period from January 1, 2006 through December 31, 2009. The examination was conducted in accordance with the National Association of Insurance Commissioners' Financial Condition Examiners Handbook. The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, to identify prospective risks, and to obtain information about the Company, including corporate governance, identification and assessment of inherent risks, and the evaluation of the system controls and procedures used to mitigate those risks. The examination also included an assessment of the principles used and the significant estimates made by management, as well as an evaluation of the overall financial statement presentation, and management's compliance with Statutory Accounting Principles and National Association of Insurance Commissioners' Annual Statement Instructions. All accounts and activities of the Company were considered in accordance with the risk-focused examination process. The examination was conducted concurrently with that of the Company's affiliate, Western Select Insurance Company.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; and sales and advertisement.

SUMMARY OF SIGNIFICANT FINDINGS

As a result of this examination, surplus as regards policyholders as of December 31, 2009 has been reduced by $2,568,445 to $16,144,739. The reduction in surplus was due to non admitting amounts due from parent, subsidiaries and affiliates that were over 90 days at the date of examination and establishing a provision for reinsurance.

SUBSEQUENT EVENTS

On January 31, 2011, in accordance with an order of the United State District Court for the Central District of California, ownership of the Company was transferred back to its former owner, National Farm Financial Corporation (NFFC). See further comments with respect to the ownership change under the Company History section. Both the Intercompany Service Agreement and the Consolidated Federal Income Tax Liability Allocation Agreement with Public Service Mutual Insurance Company (PSMIC) were canceled effective January 1, 2011. The 90% Quota Share Reinsurance Agreement with PSMIC was canceled on a cut-off basis effective 11:59 P.M. on January 31, 2011.

COMPANY HISTORY

The Company was incorporated in California on November 12, 1996, under the laws of the State of California and commenced business on September 15, 1997.

On September 16, 2005, PSM Holding Corp. (PSM) claimed that it had entered into an agreement to purchase the Company while the Company's owners claimed there was no agreement to sell the Company. On December 22, 2005, PSM filed a lawsuit (Case No. CV 05-08891 MMM (FMOx)) against the Company, its parent, National Farm Financial Corporation (NFFC), and Larry P. Chao (collectively the Defendants) in the United States District Court for the Central District of California for breach of contract, fraud and negligent misrepresentation. The trial commenced on August 14, 2007 and lasted over four weeks. On September 14, 2007, the jury found in favor of PSM.

The jury found the Defendants joint and severally liable to PSM for $40 million for breach of contract and $3 million for fraud (Verdict). Post trial motions were filed by both PSM and the Defendants. Post trial motions resulted in the court throwing out the $3 million attributed to the fraud counts and awarded PSM legal costs of $3.1 million. Judgment was entered on October 4, 2007. The Defendants filed a notice of appeal to the United States Court of Appeals for the Ninth Circuit (Court of Appeals) on February 5, 2008.

While the appeal was pending, NFFC and Larry P. Chao filed for bankruptcy. In October, 2008, pursuant to a bankruptcy court order, the Judgment was partially satisfied by NFFC transferring ownership of the Company to PSM out of the NFFC bankruptcy proceedings. This transfer was approved by both the New York and California Departments of Insurance (CDI). PSM released the Company from the Judgment as a condition of the ownership transfer.

On June 18, 2009, the Court of Appeals reversed the lower court's Judgment ordering entry of judgment in favor of NFFC and also awarded the Defendants $2,224,221 in attorney's fees and

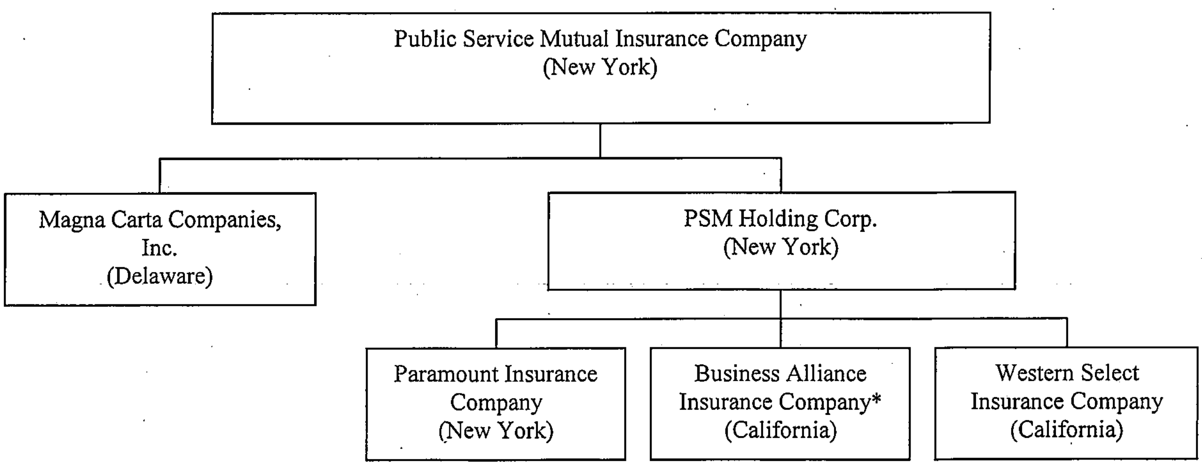
$53,985 in other costs. Thereafter, PSM filed its petition for reconsideration which was denied on July 28, 2009. Subsequently, NFFC and Larry P. Chao's bankruptcy proceedings were dismissed.

On July 26, 2010, the United States District Court for Central District of California (Court) ordered the return of the Company's shares to the Defendants and an accounting of the profits PSM generated through its ownership of those shares. The Court directed PSM to transfer ownership of the Company's shares to Defendants within sixty days. This order was later modified and the deadline to complete the transfer was extended to January 31, 2011.

PSM transferred ownership of the Company to NFFC effective the end of day on January 31, 2011 in accordance with the July 26, 2010 Order as amended. The transfer was sanctioned by the CDI as set forth in its letter of September 30, 2010.

MANAGEMENT AND CONTROL

The following organizational chart depicts the Company's relationship within the holding company system as of December 31, 2009 (all ownership is 100%):



* Due to a reversal of a lower court's judgment by the United States Court of Appeals for the Ninth Circuit, ownership of Business Alliance Insurance Company was transferred back to its former owner, National Farm Financial Corporation, effective at 11:59 p.m. on January 31, 2011.

Management of the Company is vested in a four-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2009 follows:

Directors

Name and Residence	Principal Business Affiliation
Charles L. Crouch, III La Canada, California	Senior Vice President, General Counsel, and Secretary Public Service Mutual Insurance Company
Andrew L. Furgatch Los Angeles, California	Chairman of the Board and Chief Executive Officer Public Service Mutual Insurance Company
John Hill, II Pennington, New Jersey	President, Chief Operating Officer, and Treasurer Public Service Mutual Insurance Company
David A. Lawless Mamaroneck, New York	Senior President, Chief Administrative Officer Public Service Mutual Insurance Company

Principal Officers

Name	Title
Andrew L. Furgatch	Chief Executive Officer
John Hill, II	President, Chief Operating Officer and Treasurer
Charles L. Crouch, III	Senior Vice President, General Counsel and Secretary
David A. Lawless	Senior Vice President and Chief Administrative Officer

Intercompany Agreements

Intercompany Service Agreement: Western Select Insurance Company, a Company affiliate, entered into an Intercompany Service Agreement (Agreement) with its ultimate parent, Public Service Mutual Insurance Company (PSMIC), effective May 1, 1999. The Agreement was approved by the California Department of Insurance (CDI) on March 9, 1999. Under the agreement, PSMIC makes available the services of its personnel, office space, equipment, and other services. The Company was added to the Agreement by an addendum effective October 21, 2008. This addendum was filed with the CDI and a no objection determination was issued on December 8, 2008.

The costs allocated based on shared services paid in 2009 were $326,836. There were no amounts paid in 2008.

A review of the Agreement and some of the underlying transactions indicated that there were a number of issues with the terms of the Agreement and the handling of the transactions. Although these problems existed as of December 31, 2009, no recommendations were made in this examination report to correct the problems noted, as effective January 31, 2011, PSMIC no longer is the parent of the Company.

The problems with the terms of the Agreement and its administration were as follows:

The Agreement does not contain a timely settlement provision of amounts owed with a specified due date as required by Statements of Statutory Accounting Principles (SSAP) No. 96, Paragraph 2, nor does it contain an offset provision as required by SSAP No. 64, Paragraph 5.

The intercompany balances were not being settled on a timely basis. The Agreement states: "Any premiums collected shall be held in a fiduciary capacity and shall be paid over to the Subsidiary immediately upon collection."

Direct billed premium collections for all of 2009 were collected by PSMIC but not recorded by the Company until March, 2010. Actual settlement was made in June, 2010. The amount collected by PSMIC will be reclassified as due from PSMIC at December 31, 2009. The amount over 90 days at December 31, 2009 of $2,164,000 will be non-admitted.

In December 2009, the Company recorded a liability to PSMIC for shared expenses for 2009 in the amount of $363,152. An additional liability for the same amount was also recorded in December 2009. However, there was no support for this additional liability and the Company's response was that it was for 2008 expenses. The amount could not be supported as required by the Agreement and a receivable will be established as due from PSMIC in this examination report.

PSMIC is receiving payments, paying expenses, commissions and claims of the Company and charging the Company through intercompany accounting. These services are not covered under the Intercompany Service Agreement with PSMIC. California Insurance Code 1215.5 (b) (4) requires all management agreements to be filed with the CDI.

Consolidated Federal Income Tax Liability Allocation Agreement: Public Service Mutual Insurance Company (PSMIC) and other subsidiaries entered into a Consolidated Federal Income Tax Liability Allocation Agreement (Tax Agreement), effective January 1, 2001. Effective January 1, 2009, the Company was added by an addendum to the agreement. This addendum was filed with the California Department of Insurance which issued a no objection determination on December 8, 2008. Under the terms of the agreement, PSMIC files the federal income tax return on a consolidated basis and the individual companies should not pay more than they would were if the tax calculated were on an individual basis. Any refunds which they would be entitled as were the tax was calculated on an individual basis.

The Company did not account for and settle its tax allocation transactions separately from related party transactions in accordance with the National Association of Insurance Commissioners' Annual Statement Instructions as required by California Insurance Code (CIC) Section 923.

Although this situation existed as of December 31, 2009, no recommendations were made in this examination report to correct the problem noted as effective January 31, 2011, PSMIC no longer is the parent of the Company.

CORPORATE RECORDS

The Company is not in compliance with California Insurance Code (CIC) Sections 1200 and 1201. Its minutes failed to document the authorization or approval of its investments in several instances. There were no approvals noted for investments made prior to October 22, 2008, and from October 23, 2008 through October 31, 2008. The Board also did not approve the Company's investment purchases, sales and exchanges for the period November 1, 2008 through July 31, 2009 until August 20, 2009. In addition, specific references to amounts, facts and the values of the securities were not included as required under CIC Section 1201.

It is recommended that the Company implement procedures to comply with CIC Sections 1200 and 1201.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2009, the Company was only licensed in the State of California to transact multiple lines of property and casualty insurance, but only writes commercial multiple peril insurance. Direct and net premiums written in 2009 were $7,881,198 and $788,120, respectively.

The commercial multiple peril policies are written through approximately 300 independent brokers. The Company's business owner policy is aimed primarily at small business owners. The Company maintains a processing office in San Bruno, California.

REINSURANCE

Assumed

The Company did not assume any reinsurance.

Ceded

The Company entered into a 90% quota share reinsurance agreement with its ultimate parent, Public Service Mutual Insurance Company (PSMIC), in October of 2008. The agreement applied to unearned premiums, unpaid losses and loss adjustment expense reserves as of October 1, 2008 as well as future premiums written. The Company reduced its loss and loss adjustment expense reserves by $7,769,756 at December 31, 2009. As a result of this agreement, the Company receives a 35% ceding commission on the premiums ceded. This agreement was filed and approved by California Department of Insurance (CDI) via a no objection letter on December 8, 2008.

The unaffiliated reinsurance agreements which provided excess of loss protection to the Company in excess of $300,000 were canceled as to new business effective December 31, 2008. All recoveries from these reinsurers were deposited into PSMIC's bank account and retained by PSMIC. It is the Company's position that since PSMIC was reinsuring 90% of gross liability of the Company that all recoveries should inure to PSMIC.

On risks in excess of $1 million the Company obtains facultative reinsurance.

In 2003, the Company began offering automobile mechanical breakdown policies to individuals in California. The Company ceased offering this type of policy effective January 1, 2007. The Company ceded 100% of the net liability for these policies under a reinsurance agreement, effective May 1, 2003, with National Service Contract Insurance Company RRG (NSCIC-RRG) an unauthorized reinsurer and a risk retention group that is domiciled in the District of Columbia. This arrangement was noted in the last examination as being not in compliance with California

Insurance Code Section 130(k)(7)(B), which limit risk retention groups to assuming business from other risk retention groups or other qualified members. It was recommended in the last examination report that the Company develop and submit a plan of action to the CDI regarding how it plans to comply with California laws and run-off the remaining book of automobile mechanical breakdown business. The Company did not comply with this recommendation. It is again recommended that the Company develop and submit a plan of action to the CDI with respect to how it plans to comply with California laws and run-off the remaining book of automobile mechanical breakdown business.

NSCIC-RRG secured its liability to the Company by depositing funds into a trust account for the benefit of the Company. The trust account balance totaled $983,245 at December 31, 2009. PSMIC assumed 100% of the liability of the Company as of September 30, 2008. There is no written agreement between the parties and nothing was filed with the CDI for approval. This business had already been ceded to NSCIC-RRG. Funds held by the company under reinsurance treaties as of December 31, 2009 in the amount of $983,245 is being established in this examination report as due from PSMIC since there was no formal reinsurance agreement and the fact that the business was already 100% reinsured.

As additional security, the Company reported that it holds a $250,000 letter of credit from NSCIC-RRG. The Company was not able to produce the letter of credit. Therefore, a provision for reinsurance in the amount of $67,597 has been established in this examination report which is the difference between the unearned premiums of $1,050,842 and the amount established as Funds Held by the Company under Reinsurance Treaties in the amount of $983,245.

The Company did not report the NSCIC-RRG treaty in Schedule F, Part 3 of the 2008 or the 2009 Annual Statement, nor it losses paid in its Annual Statement. It is recommended that the Company adhere to National Association of Insurance Commissioners' Annual Statement Instructions in recording its transactions with respect to its book of mechanical breakdown book of business.

The unearned premium at December 31, 2009 totaled $1,050,842 and the remaining approximately 2,900 policies will expire by 2013.

ACCOUNTS AND RECORDS

The Company combined uncollected premium (Annual Statement page 2, line 13.1) with deferred premiums (Annual Statement page 2, line 13.2) and reported both under line 13.1, which is not in accordance with National Association of Insurance Commissioners' (NAIC) Annual Statement Instructions. This was also an issue during the prior examination.

The Company combined advance and unearned premiums and reported both as unearned premiums, which is not in accordance with NAIC's Annual Statement Instructions. This was also an issue during the prior examination.

The Company reported uncollected premiums and agents' balances in course of collection net of commissions. Statements of Statutory Accounting Principles (SSAP) No. 6 requires that Uncollected Premiums be reported gross of commissions.

Reinsurance balances to and from PSMIC were reported and netted against amounts Due to Parents, Subsidiaries and Affiliates which is not in accordance with Statements of Statutory Accounting Principles No. 62 and No. 67 and the NAIC's Annual Statement Instructions, which require reinsurance balances to be reported separately as assets and liabilities. Although this situation existed as of December 31, 2009, no recommendations were made in this examination report regarding this issue as effective January 31, 2011, PSMIC no longer is the parent of the Company and the 90% Quota Share Reinsurance Agreement with PSMIC was canceled on a cut-off basis effective 11:59 P.M. on January 31, 2011.

It was recommended that the Company exercise due diligence to insure that its annual statements are completed in accordance with Statements of Statutory Accounting Principles and NAIC's Annual Statement Instructions.

In addition to the above, there were a number of findings and recommendations under the Accounts and Records section of the December 31, 2005 examination report. Because of the litigation between PSM Holding Corp. and National Farm Financial Corporation (NFFC), et al. and the change in ownership of the Company from NFFC to Public Service Mutual Insurance Company, the findings and recommendations were not addressed. As a result, the findings and recommendations are repeated below:

- It is recommended that the Company establish control procedures to detect and prevent the types of reporting errors that were noted during the examination from occurring in the future.

- It is recommended that the Company employ sufficient levels of appropriately qualified and trained personnel in the financial reporting processes.

- It is recommended that the Company have on-hand detailed policies and claims data with respect to its policyholders and claimants for its book of auto mechanical breakdown business.

- It is recommended that the Company document backup procedures in the event that its program administrator, Interstate National Dealers Services, Inc. is unable or unwilling to process the Company's claims as it relates to its book of auto-mechanical breakdown business.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2009

Underwriting and Investment Exhibit for the Year Ended December 31, 2009

Reconciliation of Surplus as Regards Policyholders from December 31, 2005 through December 31, 2009

Reconciliation of Examination Changes as of December 31, 2009

Statement of Financial Condition
as of December 31, 2009

Assets	Ledger Assets	Assets Not Admitted	Net Admitted Assets	Notes
Bonds	$ 12,721,153	$	$ 12,721,153	
Cash and short-term investments	3,078,212		3,078,212	
Other invested assets	983,245		983,245	
Investment income due and accrued	156,952		156,952	
Uncollected premiums and agents' balances in course of collection	1,463,759	43,659	1,420,100	(1)
Due from parent, subsidiaries and affiliates	3,699,594	2,164,000	1,535,594	(2)
Net deferred tax asset	342,552		342,552	
Aggregate write-ins for other than invested assets	720,450	720,450	0	(2)
Total assets	$ 23,165,917	$ 2,928,109	$ 20,237,808	

Liabilities, Surplus and Other Funds			
Losses		$ 724,220	(3)
Loss adjustment expenses		808,921	(3)
Taxes, licenses and fees		23,095	
Current federal and foreign income tax		51,822	
Unearned premiums		709,715	
Funds held by company under reinsurance treaties		983,245	(2)
Provision for reinsurance		67,597	(4)
Payable to parent, subsidiaries and affiliates		725,046	(2)
Aggregate write-ins for liabilities		(592)	(2)
Total liabilities		4,093,069	
Common capital stock	$ 2,600,000		
Gross paid-in and contributed surplus	5,490,240		
Unassigned funds (surplus)	8,054,499		
Surplus as regards policyholders		16,144,739	
Total liabilities, surplus, and other funds		$ 20,237,808	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2009

Statement of Income

Underwriting Income		
Premiums earned		$ 826,406
Deductions:		
Losses incurred	$ 652,048	
Loss expense incurred	1,052,376	
Other underwriting expenses incurred	(202,215)	
Total underwriting deductions		1,502,209
Net underwriting loss		(675,803)
Investment Income		
Net investment income earned	$ 709,612	
Net investment gain		709,612
Other Income		
Net loss from agents' balances charged off	$ (16,576)	
Finance and service charges not included in premium	162,363	
Aggregate write-ins for miscellaneous income	463,765	
Total other income		609,552
Net income before federal income taxes		643,361
Federal income taxes incurred		45,933
Net income		$ 597,428

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2008		$ 17,448,023
Net income	$ 597,428	
Change in net deferred income tax	252,220	
Change in non-admitted assets	(2,085,335)	
Provision for reinsurance	(67,597)	
Change in surplus as regards policyholders		(1,303,284)
Surplus as regards policyholders, December 31, 2009		$ 16,144,739

Reconciliation of Surplus as Regards Policyholders
from December 31, 2005 through December 31, 2009

	Gain in Surplus	Loss in Surplus	
Surplus as regards policyholders, December 31, 2005, per Examination			$ 13,041,373
Net income	$ 5,699,552	$	
Net unrealized capital gain	1,500		
Change in net deferred income tax	342,553		
Provision for reinsurance		67,597	
Change in non admitted assets		2,871,145	
Aggregate write-ins for losses in surplus		1,497	
Totals	$ 6,043,605	$ 2,940,239	
Net increase in surplus as regards policyholders			3,103,366
Surplus as regards policyholders, December 31, 2009, per Examination			$ 16,144,739

Reconciliation of Examination Changes
as of December 31, 2009

Assets	Per Company	Per Examination	Surplus Increase (Decrease)	Notes
Uncollected premiums and agents' balances in course of collection	$ 4,756,542	$ 1,420,100	$ (3,336,442)	(1)
Due from parent, subsidiaries and affiliates	0	1,535,594	1,535,594	(2)
Aggregate write-ins for other than invested assets	0	0	0	(2)
Liabilities				
Funds held by company under reinsurance treaties	0	983,245	(983,245)	(2)
Provision for reinsurance	0	67,597	(67,597)	(4)
Due to parent, subsidiaries and affiliates	1,008,291	725,046	283,245	(2)
Net decrease to surplus as regards policyholders			(2,568,445)	
Surplus as Regards Policyholders, December 31, 2009 per Company			18,713,184	
Surplus as Regards Policyholders, December 31, 2009 per Examination			$ 16,144,739	

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Premiums and Agents' Balances in Course of Collection

Direct billed premium collections for all of 2009 were collected by Public Service Mutual Insurance Company (PSMIC) and not recorded by the Company until March, 2010. Actual settlement was made in June, 2010. The net amount collected by PSMIC, $3,336,442, is reclassified as due from PSMIC at December 31, 2009.

(2) Due from Parent, Subsidiaries and Affiliates
(2) Aggregate Write-ins for Other than Invested Assets

Direct billed premium collections for all of 2009 were collected by Public Service Mutual Insurance Company (PSMIC) and not recorded by the Company until March, 2010. Actual settlement was made in June, 2010. The net amount collected by PSMIC $3,336,442 is reclassified as due from PSMIC in this examination report. The amount over 90 days at December 31, 2009 of $2,164,000 was non-admitted.

During 2008, the Company advanced $ 700,000 to National Farm Financial Corporation (NFFC) and non-admitted said advance in its December 31, 2008 Annual Statement.

In December 2009, PSMIC assumed the $700,000 advance to NFFC. There are no supporting documentation or board minutes covering this assumption. This amount has been reclassified as due to PSMIC and the advance to NFFC established as an asset in this examination report. This amount has been non-admitted.

(3) Losses and Loss Adjustment Expenses

Based on an analysis by a Casualty Actuary for the California Department of Insurance (CDI), the Company's loss and loss adjustment expense reserves as of December 31, 2009 were found to be reasonably stated and have been accepted for the purposes of this examination.

(4) Provision for Reinsurance

The amount of $983,245 has been reclassified as due from Public Service Mutual Insurance Company to Funds Held by the Company under Reinsurance Treaties in this examination report. As additional security, the Company indicated they held a $250,000 letter of credit. The Company was not able to produce the Letter of Credit. Therefore, a Provision for Reinsurance in the amount of $67,597 has been established in this examination report.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Corporate Records (Page 8): It is recommended that the Company implement procedures in its board meetings to ensure compliance with California Insurance Code (CIC) Sections 1200 and 1201.

Reinsurance - Ceded (Page 9): It is again recommended that the Company develop and submit a plan of action to the California Department of Insurance (CDI) with respect to how it plans to comply with California laws and run-off the remaining book of automobile mechanical breakdown business.

Reinsurance - Ceded (Page 9): It is recommended that the Company adhere to Annual Statement Instructions in recording its transactions regarding its book of mechanical breakdown book of business.

Accounts and Records – (Page 11): It is recommended that the Company exercise due diligence to insure that its annual statements are completed in accordance with Statements of Statutory Accounting Principles and NAIC's Annual Statement Instructions.

Accounts and Records – (Page 11):

- It is recommended that the Company establish control procedures to detect and prevent the types of reporting errors that were noted during the examination from occurring in the future.
- It is recommended that the Company employ sufficient levels of appropriately qualified and trained personnel in the financial reporting processes.
- It is recommended that the Company have on-hand detailed policies and claims data with respect to its policyholders and claimants for its book of auto mechanical breakdown business.
- It is recommended that the Company document backup procedures in the event that its program administrator, Interstate National Dealer Services, Inc. is unable or unwilling to process the Company's claims as it relates to its book of auto-mechanical breakdown business.

Previous Report of Examination

Management and Control-Intercompany Arrangements (Page 2): It was recommended that the Company comply with California Insurance Code (CIC) Section 1215.5(b) (4) and obtain approval for its licensing agreement with its parent company. It was also recommended that the Company comply with CIC Section 1215.5(b) (4) with respect to its facilities sharing agreement. Since Public Service Mutual Insurance Company (PSMIC) acquired the Company on October 21, 2008, this finding and recommendation is no longer an issue.

Territory and Plan of Operation (Page 5): It was recommended that the Company develop and submit a plan of action to the California Department of Insurance (CDI) with respect how it plans to comply with California laws and run-off the remaining book of automobile mechanical breakdown business that is still on its books. This has not been done and the recommendation is repeated in this examination report.

It was also recommended that the Company comply with the requirements of the Managing General Agent Act with respect to Interstate National Dealers Services, Inc. (INDS), the program administrator of its automobile mechanical breakdown business. Since INDS does not produce business for this line of business, it currently does not meet the definition for being a managing general agent anymore.

Reinsurance: (Page 6): It was recommended that the Company and its reinsurers work with the CDI Legal Division to clear deficiencies with respect to the special termination agreement provisions in the agreements. Since being acquired by PSMIC all unaffiliated reinsurance agreements were terminated in 2008.

Accounts and Records (Page 8): It was recommended that the Company exercise due diligence to insure that its Annual Statements are completed in accordance with Statements of Statutory Accounting Principles and NAIC's Annual Statement Instructions – Property and Casualty.

- It was recommended that the Company establish control procedures to detect and prevent the types of reporting errors that were noted during the examination from occurring in the future.

- It was recommended that the Company employ sufficient levels of appropriately qualified and trained personnel in the financial reporting processes.

- It was recommended that the Company have on-hand detailed policies and claims data with respect to its policyholders and claimants for its book of auto mechanical breakdown business.

- It was recommended that the Company document backup procedures in the event that its program administrator, Interstate National Dealers Services, Inc is unable or unwilling to process the Company's claims as it relates to its book of auto-mechanical breakdown business.

The Company has not corrected these findings and recommendations. These recommendations are again repeated in this report either under the Reinsurance or Accounts and Records sections.

Accounts and Records – Information System Controls (Page 11): It was recommended that the Company review the comments and recommendations and institute control procedures to strengthen its internal control over its information system. Since being acquired by PSMIC, the Company has resolved this issue by virtue of its business being moved onto a new computer system and automation platform.

Comments of Financial Statement Items – Losses and Loss Adjustment Expenses (Page 16): It was recommend that the Company institute control procedures and perform monthly reconciliations to insure that the Company's loss data is accurately reflected across all systems that maintain loss data and loss transactions. Since being acquired by PSMIC, the Company has resolved this issue by virtue of its business being moved onto a new computer system and automation platform. PSMIC reviewed every claim file and re-entered the data onto its own system.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Company's officers and parent's employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

______________/S/______________

William Fisher, CFE
Examiner-In-Charge
Contract Insurance Examiner
Department of Insurance
State of California